



DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

OFFICE OF
CHIEF COUNSEL

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The Honorable Richard G. Lugar
United States Senate
Washington, D.C. 20510-1401

3121.00-00

Attention: Darlee McCollum

Dear Senator Lugar:

I am responding to your letter dated April 12, 2000, to Mr. Floyd Williams, National Director for Legislative Affairs, on behalf of [REDACTED]

[REDACTED], about the lack of a totalization agreement between the United States and Puerto Rico.

[REDACTED] sometimes sends U.S. employees to work temporarily at the facilities of its Puerto Rican affiliate. [REDACTED] wants to use a "split-pay" arrangement for these employees, under which part of the employee's pay (including all the benefits) would be paid by [REDACTED] and part by [REDACTED]'s Puerto Rican affiliate. [REDACTED] believes a totalization agreement would enable Lilly to create a split-pay arrangement. He indicates a special problem in the area of 401(k) contributions, because the Puerto Rican contribution limit is lower than the U.S. limit.

Totalization Agreements Coordinate Two Social Security Systems

A totalization agreement coordinates the U.S. social security system with the social security system of a foreign country in two ways. First, the agreement eliminates double social security taxation for active workers from one country who are working in the other country. Second, the agreement allows work credits under both systems to be combined to determine if an individual is entitled to social security benefits after he or she quits working. This enables workers who would not be eligible for regular benefits from either country to receive "totalization" benefits based on their combined work record. The United States currently has seventeen social security totalization agreements with foreign countries.

There is No Need for a Totalization Agreement with Puerto Rico

Although Puerto Rico is generally treated as “foreign” for federal income tax purposes, section 3121(e) of the Internal Revenue Code provides that Puerto Rico is treated as part of the United States for purposes of the social security tax. Puerto Rican employers are required to withhold and pay tax into the U.S. social security system. Our existing totalization agreements are all with foreign countries that maintain their own social security systems. Those agreements are needed to ensure individuals from one country who are working in the other country will not be required to pay social security tax to both countries and will receive work credits toward retirement based on their entire work record. Puerto Rico has no separate social security system that would need to be coordinated with the U.S. system. Therefore, a totalization agreement with Puerto Rico is not necessary.

Section 401(k) Contribution Limits

We cannot respond to the taxpayer’s concern about 401(k) contribution limits, because we do not understand the link between a totalization agreement and 401(k) contribution limits. The two appear to be unrelated. If your office can obtain more information about the exact nature of the concern, I would be happy to address it.

I hope this information is of assistance to you. As requested, I am sending this reply in duplicate and returning your enclosure. If you have any questions, please contact me or Grace Fleeman at (202) 622-3880.

Sincerely,

Elizabeth U. Karzon
Chief, Branch 1
Office of the Associate Chief Counsel (International)

Enclosures (3)